
IN THE
United States
Circuit Court of Appeals,
FOR THE NINTH CIRCUIT.

Belridge Oil Company, a corporation,
Petitioner and Appellant,
vs.
Commissioner of Internal Revenue,
Respondent.

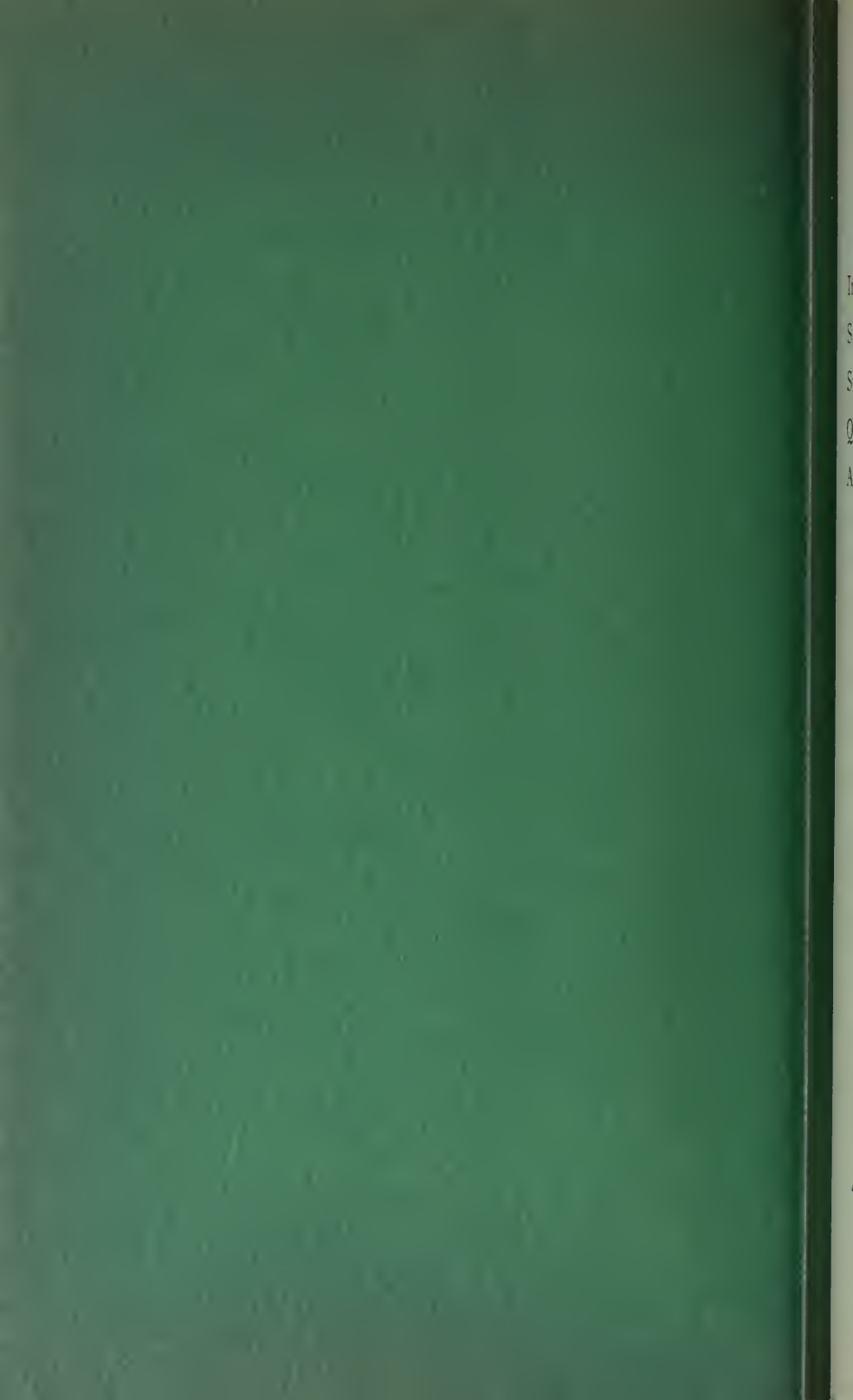
BRIEF FOR PETITIONER AND APPELLANT.

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No. 7103.

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Commissioner of Internal Revenue,
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BRIEF FOR PETITIONER AND APPELLANT.

INTRODUCTION.

This is an appeal from a final order of the United States Board of Tax Appeals affirming the action of the Commissioner of Internal Revenue in determining that there is a deficiency in petitioner's income and excess profits tax for the calendar year 1921 in the amount of \$45,293.85.

On July 18, 1927, in accordance with the provisions of section 274 of the Revenue Act of 1926, the Commissioner of Internal Revenue, respondent herein, notified the petitioner that his investigation of the income tax return of

petitioner for the year 1921 disclosed a deficiency in income and excess profits tax in the amount of \$45,293.85. From this determination the petitioner duly filed its appeal to the United States Board of Tax Appeals. Thereafter, on May 22, 1930, the proceeding came to trial before the Board, the Honorable Stephen J. McMahon, member, presiding. On August 16, 1932, the Board promulgated its findings of fact and opinion in said appeal and on August 17, 1932 the Board entered its final order of redetermination sustaining the Commissioner's determination. Said opinion is reported in 26 B. T. A. 810. Appeal from this order is brought to this court by petition for review filed November 15, 1932, pursuant to the provisions of sections 1001-1003 of the Revenue Act of 1926 as amended by section 1101 of the Revenue Act of 1932.

STATUTE INVOLVED.

Section 326 (a) of Revenue Act of 1921:

"Sec. 326 (a) That as used in this title the term 'invested capital' for any year means:

(1) Actual cash *bona fide* paid in for stock or shares;

(2) Actual cash value of tangible property, other than cash, *bona fide* paid in for stock or shares, at the time of such payment, but in no case to exceed the par value of the original stock or shares specifically issued therefor, unless the actual cash value of such tangible property at the time paid in is shown to the satisfaction of the Commissioner to have been clearly and substantially in excess of such par value in which case such excess shall be treated as paid-in surplus: * * *"

STATEMENT OF FACTS.

In 1910 and prior thereto one, Emily B. Hopkins, now deceased, owned 30,845.96 acres of land, in an unbroken parcel located in Kern county, California, between McKittrick and Lost Hills. [R. 65.] Mrs. Hopkins did not personally manage this property but lived in New York and left the management to her agents, C. A. Grove, the Stearns Rancho Co. and one William Hill. [R. 65-66.] In 1910 one, W. J. Hole, who had had considerable experience as a real estate dealer in California and who had been resident agent for the Stearns Rancho Co. [R. 64] by reason of his former association with Mrs. Hopkins and her agents, was able to secure an option from her for the purchase of said 30,845.96 acres of property for \$20 per acre. [R. 66.] Hole desired this option for the reason that he thought it valuable agricultural land and that since it was located between oil producing properties it might be valuable as oil property. [R. 67.] Hole, however, was not an experienced oil man and, to his knowledge, the property was virgin territory for oil purposes. [R. 67.]

During the year 1910, one William Van Slyke, who was an experienced oil operator [R. 76] had occasion to go upon the Hopkins property. [R. 77.] He noticed outcroppings upon the land which were similar to outcroppings upon proven oil land. [R. 77.] He later returned to the property, dug a 14 foot hole and discovered oil sands which he tested and which proved to be live oil sands. [R. 77.] He covered the hole with planks and brush, so that it would not be discovered. [R. 78.] Van Slyke informed one, Max Whittier, now deceased, of his discovery and was advised by Whittier not to disclose the information to any one and that Whittier would

attempt to acquire some of the land. [R. 78.] Whittier also visited the property with Van Slyke. [R. 78.]

About this time Hole approached Whittier, whom he knew to be an experienced oil man, told him that he had an option to purchase the Hopkins property and offered to sell the property to Whittier for $\$33\frac{1}{3}$ per acre and a one-fifth interest in any company organized to take it over. [R. 67 and 83.] Hole did not tell Whittier of the terms of his option [R. 69] and Whittier did not tell Hole of Van Slyke's discoveries upon the property. [R. 70.] Whittier took Hole to interview one, Burton E. Green, an experienced and successful oil man and an associate of Whittier, who had been informed of Van Slyke's discovery and who was familiar with the general territory. [R. 67 and 83.] At this interview Whittier and Green agreed to take the option if it could be revamped to allow them to drill for oil before exercising the option. [R. 83.]

Hole started negotiations to secure the new option and in order to do so was forced to enlist the services of one, Benedict, a cousin of Mrs. Hopkins, and her agent, William Hill. Hole paid Benedict \$125,000 and Hill \$35,000 and one-fourth of Hole's stock in petitioner for their services in securing the option. [R. 69.] The option desired was finally secured on Jan. 5, 1911 and it provided very favorable terms for the drilling of the test wells before exercising the option and for the sale of the property to Hole for $\$33\frac{1}{3}$ per acre. The consideration paid to Mrs. Hopkins for the option was \$25,000 [Ex. 1, R. 155], which \$25,000 was furnished by Green. [R. 100.]

Petitioner was organized in January, 1911 and on January 25, 1911, Hole assigned the option of January 5,

1911 to petitioner in exchange for 999,995 shares of stock of petitioner. [Ex. 3, R. 168-170.] Hole retained one-fifth of the stock and immediately transferred the balance to Whittier, Green, M. J. Connell and Frank Buck, the latter two men having been taken into the deal. [Ex. 4, R. 171-172.]

According to the "logs" of the first and second wells begun on March 11 and March 18, 1911, respectively, and completed on April 21, 1911, and April 7, 1911, respectively, oil sand was first struck at between 445 and 480 feet and it produced 100 barrels of oil per day, 25.3 degrees Baume, thirty days after completion, and oil sand was struck in the second well at between 350 and 360 feet and it produced 100 barrels per day, 26.5 degrees Baume, thirty days after completion. [Exhibit 5, R. 172.]

Petitioner contends that the option on the Hopkins property of January 5, 1911, had an actual cash value at January 25, 1911 in excess of the par value of the stock issued for it on that date. Respondent contends that the said option had an actual cash value at January 25, 1911 of only \$25,000 and has excluded from petitioner's invested capital for 1921 "Stock discount \$974,995", representing that portion of the par value of capital stock \$999,995, issued in 1911 for the option upon the Hopkins property, in excess of \$25,000. The Board of Tax Appeals in its decision, 26 B. T. A. 810, upheld the determination of the respondent.

QUESTIONS PRESENTED.

As stated by the Board of Tax Appeals in its opinion [R. 26], the sole question presented for its determination was “the ‘actual cash value’ of the option ‘at the time of’ its payment for the capital stock of petitioner on January 25, 1911. (Section 326 of the Revenue Act of 1921.) It is conceded by counsel for the respondent that if the value of the option is satisfactorily substantiated there is no question about its inclusion in invested capital to the extent justified by the proof”.

The present appeal presents to this Honorable Court for consideration the following questions:

1. Was the finding and opinion of the Board Member that the “actual cash value” of the option on January 25, 1911 did not exceed \$25,000.00 supported by substantial evidence?

2. Did the Board Member err in disregarding the testimony of petitioner’s expert witnesses and other competent evidence as to the actual cash value of the option on January 25, 1911?

3. Did the Board Member err in failing to conclude under all the evidence that the option had an actual cash value on January 25, 1911 of at least \$1,000,000.00?

ASSIGNMENTS OF ERROR.

(1) The United States Board of Tax Appeals erred in making and entering its decision in this cause and in entering judgment in favor of Commissioner and against taxpayer.

(2) The United States Board of Tax Appeals erred as a matter of law and fact in deciding that the option which

taxpayer acquired on January 25, 1911, had only a value, for invested capital purposes, of \$25,000.00.

(3) The United States Board of Tax Appeals erred as a matter of law, in disregarding the competent testimony of qualified witnesses that the option which taxpayer acquired on January 25, 1911, had an actual cash value of at least \$1,000,000.00 for invested capital purposes.

(4) The United States Board of Tax Appeal erred in its conclusions of law and its application of the law to the facts.

(5) The United States Board of Tax Appeals erred in that the decision, opinion and order of the Board are contrary to the evidence and are not supported by the evidence.

(6) The United States Board of Tax Appeals erred in redetermining a deficiency against this taxpayer for the year 1921 amounting to \$45,293.85.

(7) The United States Board of Tax Appeals erred in that there is neither in the findings of fact by the Board nor in the opinion by the Board, any findings of fact to sustain the Board's conclusions of law as set forth in the Board's opinion and decision.

(8) The United States Board of Tax Appeals erred in that its conclusions of law stated in its opinion are contrary to and not in harmony with the Board's findings of fact.

(9) The United States Board of Tax Appeals erred in that the opinion and decision of the Board, based upon the Board's findings of fact, are contrary to law.

1. Whether the Findings of Fact and Opinion of a Member of the United States Board of Tax Appeals Are Supported by Substantial Evidence Is a Question of Law and a Proper Question for This Court to Determine Upon a Petition for Review.

This proceeding to review the decision of the United States Board of Tax Appeals presents the question to this court of whether the findings of fact and the decision of a member of the Board are supported by substantial evidence. It is now well settled by the decisions of this court as well as decisions of other Circuit Courts of Appeal that whether the findings of fact of the Board of Tax Appeals are supported by substantial evidence is a question of law and a proper question for review by the Circuit Court of Appeals. And it has also been held that when the findings of fact and decisions of the Board are not supported by substantial evidence, the decision must be reversed and set aside.

See:

Buena Vista Land and Development Company v. Lucas (C. C. A. 9), 41 Fed. (2d) 131;

Citrus Soap Company of California v. Lucas (C. C. A. 9), 42 Fed. (2d) 372;

Royal Packing Company v. Commissioner (C. C. A. 9), 22 Fed. (2d) 536;

Planters Operating Company v. Commissioner of Internal Revenue (C. C. A. 8), 55 Fed. (2d) 583;

Boggs and Buhl v. Commissioner (C. C. A. 3), 34 Fed. (2d) 859;

Chicago Railway Equipment Company v. Blair (C. C. A. 7), 20 Fed. (2d) 10;

Washburn v. Commissioner (C. C. A. 8), 51 Fed. (2d) 949;

Dempster etc. Company v. Burnet (Ct. App. D. C.), 46 Fed. (2d) 604;

Conrad and Company v. Commissioner (C. C. A. 1), 50 Fed. (2d) 576;

Pittsburgh Hotels Company v. Commissioner (C. C. A. 3), 43 Fed. (2d) 345.

2. Findings of Fact and Opinion of a Member of the United States Board of Tax Appeals Are Not Entitled to as Much Weight When the Member Dissents Who Heard the Testimony.

As a general rule, the findings of fact of the United States Board of Tax Appeals or of any trier of facts are entitled to considerable weight on appeal for the reason that the trier of facts has had an opportunity to pass upon the credibility of the witnesses and the weight to be given their testimony and the Board or trier of facts which hears such testimony is in a better position to determine the weight to be given the same than is a court which merely has access to the record. It is submitted, however, that this general rule does not apply in the case at bar where the only member of the Board who heard the testimony files a vigorous dissenting opinion and especially is this true as in the case at bar where the dissenting member in his dissenting opinion states that he was highly impressed by the intelligence, sincerity and integrity of the witnesses.

The member of the Board who rendered the decision in the case at bar was not present at the trial of this cause

and had no better means of determining the sufficiency and credibility of the testimony than has this court. The decision in the case at bar cannot be upheld upon the ground that the testimony was not reliable nor that the credibility of the witnesses is in issue for the member of the Board who heard the case found no cause to doubt the testimony in this regard and in his opinion specifically refers to “the candor, earnestness, sincerity and intelligence” [R. 38] with which the witnesses testified. Neither can it be said that the member who wrote the opinion under review exercised his independent judgment and determined the case based upon his expert knowledge and training for in the majority opinion it is stated—“* * * nor, have we substituted our own ‘knowledge, experience, and judgment’ for the opinion of these experts”. [R. 37.]

The Circuit Court of Appeals for the Second Circuit had presented to it a similar situation in the case of *Jewett and Company v. Commissioner*, 61 Fed. (2d) 471, and that court had the following to say where the dissenting member heard the testimony:

“It was of course possible for the Board to discredit the witness altogether. He was highly interested, and might well stretch the facts in his favor, especially upon a matter of opinion. *Uncasville Mfg. Co. v. Com’r.*, 55 Fed. (2d) 893, 897 (C. C. A. 2). But this was scarcely such; the patterns were used, or they were not; and the witness knew the facts. Even so, had the Board discredited him, we might accept it, since one member at least is always present when the testimony is taken. In the case at bar it was this member, however, who dissented, so that the decision cannot rest upon the appearance of the witness. But neither the findings nor the opinion sug-

gest that the witness was discredited, and we have as much before us as those members who decided the case. Upon the cold record it seems to us that the evidence is uncontradicted that all the patterns were in some use during the years in question. The Commissioner's ruling was certainly wrong; and whether the use was little or not, the depreciation charge should be fixed upon a base calculated upon the whole cost or value. If so, there was no deficiency."

In view of the fact that the question presented here is one of fact and the member who heard the testimony not only dissented but filed a very convincing dissenting opinion, it is submitted that the decision and finding of the member who wrote the opinion is not entitled to as much weight as would be true under contrary circumstances. In fact it is most extraordinary that the member who heard the testimony should not prevail with respect to the decision rendered.

3. The Findings of Fact and Opinion of the Member of the Board of Tax Appeals Is Not Supported by the Evidence.

(a) FALLACIES IN FINDINGS AND OPINION OF BOARD MEMBER.

Since the findings of fact and conclusions of the member of the Board were based entirely upon the record and since they vary quite widely from the conclusions of the dissenting member as well as from the testimony of record, the following analysis of the findings of fact and opinion of the member of the Board is here presented with corresponding marginal references to the record and to the dissenting opinion of the member who heard the testimony.

*Findings of Fact and
Opinion of Member of
Board of Tax Appeals*

1. The transaction between Hole and Mrs. Hopkins was an arm's length transaction. [R. 28.] Mrs. Hopkins' representatives took proper precautions to protect her interests. [R. 29.]

2. a—Associated Oil Company's property was more favorably situated than the Belridge property. [R. 29-30.]

*Transcript of Record and
Dissenting Opinion*

1. *Record*—Hole secured option through one Benedict, a cousin of Mrs. Hopkins, to whom he paid \$125,000 and one Hill, an agent of Mrs. Hopkins to whom he paid \$35,000 cash and one-fourth of Hole's stock in petitioner. [R. 69.] Hole had a business relationship with Mrs. Hopkins which made it possible for him to receive preferential treatment. [R. 66.]

Dissenting Opinion—The parties did not have equal knowledge of the facts. Mrs. Hopkins' representatives were not acting for her best interests. The transaction was not an arm's length transaction. [R. 41-43.]

2. a—*Record* — Witness Johnson testified that Associated Oil Company's property was less valuable for oil than the Belridge property. [R. 129-130.] Petitioner's Exhibit 6 [R. 172] shows that Belridge property was more favorably located as to producing areas and anticlines.

b—No evidence of state of development of Associated property at time of purchase.

Dissenting Opinion—Associated property not as valuable or as favorably located for oil as Belridge property. [R. 45.]

b—*Record*—Witness Johnson testified that the closest oil production to Belridge property in 1911 was in Temblor Range Field, five miles south and Lost Hills, five miles north. [R. 115.] Associated property described in Petitioner's Exhibit 2 [R. 156] when located on Petitioner's Exhibit 6 [R. 172] is shown to be in the area in which there was no oil production.

Dissenting Opinion—"The maps, Petitioner's Exhibit 6, demonstrate that none of that property (Associated) was developed as oil land previous to 1911 and that previous to 1911 there were no indications of oil or gas upon that land. [R. 45.]

3. Whittier's offer of \$500,000 for Connell's one-fifth of capital stock of petitioner was not a definite offer. [R. 30.]

3. *Record*—Connell testified that Whittier made a definite offer of \$500,000 for his interest in the stock of petitioner and such offer was made before development for oil on the Belridge property. [R. 105.]

Green testified that Whittier offered Connell \$500,000 for his interest. [R. 88.]

4. Green's valuation based only upon hearsay knowledge of other sales and what he thought other companies would have paid had they possessed the information which he had. [R. 31.]

4. *Record*—Green had extensive experience in purchasing oil property both for himself and corporations. [R. 79-81.] He was familiar with property in question and surrounding properties. [R. 82.] He examined the property in 1911. [R. 82.] His valuation was based upon his experience, his knowledge of oil properties and what was paid for them, his knowledge of the property in question and what he would have been willing to pay at that time—opinion not based purely on hearsay. [R. 102.]

Dissenting Opinion—Witness Green was intelligent, candid and well qualified. [R. 38-46 and 50.]

5. a—Johnson visited property two weeks before hearing to qualify himself as witness. [R. 31 and 34.]

5. a—*Record*—In 1907 and 1908 Johnson surveyed this general vicinity for the United States Government and made report of this land as oil bearing property. [R. 114.] He was acquainted with Belridge property in 1910 and 1911. [R. 114.]

Dissenting Opinion — In 1911, Johnson was informed

as to condition of property.
[R. 47.]

b—Johnson's valuation was based upon his education and experience as geologist.

b—*Record*—In addition to being a geologist and being familiar with the property in question, Johnson was in 1910 and 1911 actively engaged in the business of advising persons in regard to the purchase of oil properties. [R. 122.] Persons bought and sold property based upon the opinion of Johnson. [R. 122.] His opinion was based upon his experience in dealing with oil properties as well as his education and experience as a geologist. [R. 128.]

Dissenting Opinion—Johnson was well qualified. [R. 47-48 and 49.]

6. Orcutt visited property a week before hearing and based testimony on structure of land and his scientific education and experience. [R. 32 and 34.]

6. *Record*—Orcutt has been in oil business since 1897. [R. 131.] In 1910 and 1911 he advised Union Oil Co. with respect to its purchases and leases. [R. 132.] In 1910 and 1911 he was familiar with property around Belridge property. [R. 132.] Orcutt inspected Belridge property shortly before trial to confirm facts and conditions known to him in 1911. [R. 132.]

Dissenting Opinion—Orcutt well qualified. [R. 48-49.]

7. Record before Board upon which decision was made in 11 B. T. A. 127 was the same in all essential respects as record in case at bar. [R. 28.]

8. Witness for petitioner testified to theoretical value, given twenty years after transaction and based upon geological observations. [R. 34, 36.]

7. *Record and Dissenting Opinion*—Member who wrote opinion in case at bar agrees that the decision in 11 B. T. A. 127 is not *res adjudicata* of the case at bar. [R. 26.] In the Dissenting Opinion at R. 51, 52, 53, 54, 55 it is conclusively shown that additional and important evidence was adduced which was not in evidence when the decision was reached in 11 B. T. A. 127.

8. *Record*—Witness Johnson did not base estimate on a theoretical basis but upon knowledge had in 1911 of conditions and sales of property. [R. 127.] Witness Orcutt did not give estimate on theoretical basis but upon knowledge had in 1911 of actual conditions. [R. 134.] Both Johnson and Orcutt gave estimates using their geological training as well as actual experience in advising with respect to sales. [R. 128 and 134.]

Both Johnson and Orcutt closed their minds in giving estimates of value and developments subsequent to 1911. [R. 128 and 134.] Witness Green thoroughly familiar with property in 1911 and

opinion based upon extensive trading and experience in buying and selling oil properties. [R. 102.] Green determined value of property at \$100 per acre prior to the time the corporation secured the option in 1911. [R. 92.]

Dissenting Opinion—The Dissenting Opinion refutes statements that opinions were based upon theoretical estimates and primarily on geological training.

See Dissenting Opinion as to Johnson [R. 47]; Orcutt [R. 48]; and Green [R. 46].

It is submitted that pursuant to the above marginal analysis the opinion of the Board Member erroneously interpreted the record and the testimony in many vital respects. The opinion differs widely in its findings and conclusions from the findings and conclusion as made by the member who heard the testimony and who filed a dissenting opinion. It is submitted that the findings and conclusions of fact of the member who presided at the hearing and who heard the testimony are entitled to much greater weight than the conclusions of a member who reviewed the record and prepared the opinion and had no opportunity to observe the witnesses at the trial of the case. It is at once apparent from the opinion of the Board Member that scant credibility was given to the

testimony of the witnesses and this despite the fact that each of the witnesses was familiar with the property in the year 1911 and was well qualified in all respects to express an opinion as to the value of the property in question. The qualifications, intelligence and integrity of the witnesses was unchallenged at the trial of this cause. Their testimony was logical and their opinions are supported by reason and stand uncontradicted. There was practically no cross-examination of witnesses for petitioner and the cross-examination that did occur did not weaken in any important particular the testimony as given. In addition thereto, no evidence whatsoever was offered on behalf of the Commissioner of Internal Revenue at the trial of this case. Such being the facts, it is respectfully submitted that the Board member who wrote the opinion in this case erred in disregarding the testimony of the witnesses as adduced.

See:

Royal Packing Co. v. Commissioner, 22 Fed. (2d) 536;

Buena Vista Land & Development Co. v. Lucas, 41 Fed. (2d) 131;

Citrus Soap Co. v. Lucas, 42 Fed. (2d) 372;

Planters Operating Co. v. Commissioner, 55 Fed. (2d) 523;

Pittsburgh Hotels Company v. Commissioner, 43 Fed. (2d) 345;

Bonwit, Teller and Company v. Commissioner (C. C. A. 2), 53 Fed. (2d) 381.

(b) THE BOARD MEMBER DETERMINED VALUE BY AN
ERRONEOUS METHOD.

The Board Member in rendering his decision has apparently disregarded all evidence presented and rests his decision entirely upon the fact that Mrs. Emily Hopkins granted an option to one Hole for the sum of \$25,000.00. The Board Member seemed to be of the opinion that since here was evidently a cash consideration for the option, no other evidence of value could be authoritatively considered by him regardless of the fact that the particular consideration may not have represented a fair sale or an arm's length transaction or that the property as to which the option was given had a much greater value when the same was secured by the corporation and it exchanged its capital stock for the same.

The vital question is of course the value of the option at the date the corporation issued its shares of stock for the same. It is a well established fact that values for prospective oil lands may violently fluctuate over night. The organizers of the petitioner corporation were in full possession of information which demonstrated the option to be of very great value and largely in excess of the price called for in the option agreement of January 5, 1911. [Exhibit 1, R. 144.] Regardless of what price may have been paid Mrs. Hopkins, the same is not an absolute criterion of value in the hands of the corporation. And it is submitted it was error to disregard all of the surrounding and attendant circumstances and determine a value only in the amount called for in the option agreement of January 5, 1911. The value of the option would undoubtedly be admitted had the corporation issued its stock for it during March, 1911 when drilling for oil was

under way. The fact that only a month or so before, to-wit, on January 25, 1911, the stock was issued for the option, should not change the fact that it is susceptible of proof that the value was inherent in the option and that the stockholders were justified in the amount of stock which was issued for the same.

It must be borne in mind that there is in the instant case no question of an attempt to evade a higher tax because all of the transactions here in question happened long before the incidence of the Sixteenth Amendment to the Constitution which permitted the imposition of an income tax and the good faith of the entire transaction is questioned by no one. It cannot be supposed that the stockholders in organizing this corporation in 1911 had even the remotest idea that the issuance of capital stock would become important in the computation of invested capital with respect to the year 1921. The state of California sanctioned the issuance of capital stock for the option and the presumption is that the petitioner corporation acted lawfully instead of unlawfully in the issuance of its stock and that the option possessed a value equal to the value of the stock issued therefor. Cf. *Sioux City Stock Yards Co. v. Commissioner*, 59 Fed. (2d) 944, and *Rookwood Pottery Co. v. Commissioner*, 45 Fed. (2d) 43.

It is true that the Board Member who wrote the opinion in this case did decide that the option price obtained by Mrs. Hopkins from Hole was a fair one and that it was an arm's length transaction. But as convincingly set forth in the dissenting opinion [R. 41-43], such conclusion is contrary to the evidence. The evidence is clear that Mrs. Hopkins did not personally manage her property; that she lived in New York [R. 66] and left the manage-

ment of her property entirely to her agents, including one William Hill. [R. 65.] It is further clear that W. J. Hole who secured the option from Mrs. Hopkins was not experienced with respect to oil property and that when he obtained the option, he was not aware of the definitely favorable discoveries of oil sands that had been made on the property of Mrs. Hopkins by one Van Slyke. [R. 70, 83.] It is fair to conclude from the record that neither Mrs. Hopkins nor her agents had knowledge with respect to the oil producing possibilities of the land in question and the dissenting opinion points out that the clear inference is that they had no such knowledge. [R. 41.] The record is singularly clear on the other hand that Whittier and Green who furnished the money for securing the option were experienced oil men and had verified the discoveries of Van Slyke and reached definite and concrete conclusions as to the value of the land in question. Thus it cannot be said that all parties to the transaction were in possession of equal knowledge either as to property or values.

Further, the negotiations with Mrs. Hopkins were carried on through W. J. Hole. [R. 69.] Hole, by reason of business relations with Mrs. Hopkins, was in a position to obtain peculiarly favorable terms with respect to the option. [R. 65 and 66.] The securing of the option was not an arm's length transaction as the evidence shows that the same was secured through the services of one Benedict, a cousin of Mrs. Hopkins, and that Benedict was paid by Hole the sum of \$125,000.00, for his services in securing the option from Mrs. Hopkins for Hole. [R. 69.] Further, William Hill, who was the agent of Mrs. Hopkins in California, was paid the sum of \$35,000.00 in cash by

Hole, and Hole further agreed to give to Hill one-fourth of the shares of stock of the petitioner which Hole was to receive, both considerations being for the services which Hill rendered to Hole. We thus have an out of pocket expense by Hole to Benedict and Hill of the sum of \$160,000.00, and the agreement to give Hill one-fourth of the stock which Hole was to receive. In view of these facts, it seems readily apparent that the same was not a "fair sale" and was not an "arm's length" transaction, and the presumption of the Board Member to the contrary is not supported by the evidence.

It is true that the price paid for property, if the same be representative of a fair sale, is convincing evidence as to the value of the property, but such sale must be a fair one and not open to the attacks that obtain in the case at bar.

See:

Walter v. Duffy (C. C. A. 3), 287 Fed. 41;

Phillips v. United States, 12 Fed. (2d) 598;

Heiner v. Crosby (C. C. A. 3), 24 Fed. (2d) 191.

Furthermore, even if the opinion of the Board Member be taken at its full value, the member nevertheless erred in disregarding all the evidence and basing his determination solely upon the sale, for such a sale can never be made the sole basis for the determination of the value of property exclusive of other and more convincing circumstances and facts.

See:

North American Telegraph Company v. Northern Pacific Railway Company (C. C. A. 8), 254 Fed. 417;

Walls v. Commissioner (C. C. A. 10), 60 Fed. (2d) 347.

It is respectfully submitted that the circumstances hereinbefore set forth surrounding the procuring of the option are sufficient to render the price specified therefor of no evidentiary value and that the Board Member erred in basing his decision entirely upon such a sale and of making it the sole basis for his determination of the value of the option in question.

4. Value Claimed by Petitioner Was Established by the Evidence.

The decision of the Board Member cannot find support by reason of the lack of competent evidence introduced on behalf of petitioner for the record is replete with uncontradicted evidence which sustains a value for the option of at least \$1,000,000.00.

SUMMARY OF EXPERT TESTIMONY.

Petitioner presented three expert witnesses to testify with respect to values, all of whom were successful and responsible business men of Southern California, and each of whom had had a long and varied experience with respect to oil properties and the dealing in oil properties, both from the standpoint of purchase and sale, during the year 1911 and were familiar with values of oil property and pros-

pective oil properties in the year 1911 and were accordingly qualified to express an opinion as to the value of the option here in question in the year 1911. Each of these three expert witnesses were not giving a retrospective appraisal based upon information, training or experience which they had acquired since 1911, but were fully qualified in 1911, had the case arisen in that year, to give the identical testimony which they did give when this case was called for trial.

The Witness Burton E. Green.

Burton E. Green has been continuously and actively engaged in the oil business and in the purchase of oil properties in Southern California since 1895. [R. 70.] He purchased and developed many oil properties in Southern and Central California, both individually and on behalf of corporations with which he was actively identified, in and around the year 1911. [R. 79, 81.] He organized several oil companies, including the Associated Oil Company and had been on the Executive Committee of the Associated Oil Company. [R. 80.] While with the Associated Oil Company he had initiated and approved sales of oil lands. He was familiar with the development of oil property in the vicinity of the Hopkins property and had developed part of the McKittrick field during and prior to the year 1911. [R. 82.] In 1910 he was familiar with the property owned by Mrs. Hopkins. [R. 82.] He was informed of the discoveries made on the Hopkins property by Van Slyke and went upon the property and saw the oil croppings and the trench which had been dug on the Hopkins property by Van Slyke in the year 1910. [R. 82.] Witness Green testified that the fair cash value

of the property as of January 25, 1911 was \$100.00 per acre [Rr. 37], or approximately \$3,100,000.00 for the property. [R. 89.] This value was determined by the witness Green upon the basis of his experience, his knowledge of oil properties and prospective oil properties and what he had paid for them, what other corporations and individuals had paid for them, and his knowledge of the particular property in question. [R. 102.]

On the cross-examination of the witness Green, counsel for the Commissioner asked and received the following replies:

“Q. At what time did you reach the conclusion in your mind that the land was worth \$100.00 per acre?
A. Well, before we actually secured it.

Q. Well, what do you mean by saying you secured it? A. When we had the option signed up.”
[R. 92.]

Thus the opinion as to value expressed by the witness Green was one determined by him in 1911 and before the corporation secured the option in question.

The witness Green further testified that in 1911 he would have paid as high as \$100.00 per acre for the Hopkins property if it had been necessary for him and his associates to do so in order to secure the same. [R. 87.] The Board member passes over the testimony of Green with the statement, by inference at least, that it should be discounted because he was an interested party [R 34.] There is nothing in the record to indicate that the witness Green’s testimony or opinion was in any way affected by his interest in petitioner, and the presumption is that his testimony was not colored by his interest in petitioner,

especially when the member who heard the case found that the witness was both candid and sincere. [R. 38.] If the witness Green, which we submit he was, is qualified from training, experience and knowledge to express an opinion as an expert, no disqualification rests upon his testimony by reason of the fact that he was associated or connected with the petitioner. The mere fact that the witness Green might be an interested party does not disqualify him nor justify the Board in disregarding his testimony.

Dempster Mill Manufacturing Company v. Burnet,
46 Fed. (2d) 604.

The Witness Harry R. Johnson.

Harry R. Johnson is and was during the year 1911 a consulting petroleum geologist. His academic training was obtained at Stanford University and he received a degree from that University. [R. 113.] Both before and after his graduation from Stanford University the witness Johnson was employed by the United States Government in connection with geological surveys of mineral properties and was so engaged prior to the year 1911. [R. 113.] He made several geological surveys of oil properties in Central and Southern California during the years 1907 and 1908 and submitted a survey, and prepared a map, as well as, a report of the area in which the Hopkins property was located. This report was published prior to 1911 by the United States Government and is an official publication of the latter. [R. 114.] The witness Johnson was familiar with the Hopkins property

in 1910 and 1911. [R. 114.] The witness Johnson, after his resignation from the service of the United States Government in the year 1909, became actively engaged, and has been continuously since that time, engaged in the business of advising prospective purchasers of oil lands as to the value thereof and this was his profession and occupation during the year 1911. [R. 122.] Prior to the hearing of this case by the Board of Tax Appeals, the witness again went on the property with one Van Slyke and verified the discoveries which Van Slyke stated that he made in 1910 and 1911. [R. 123.] The witness Johnson did not, as might be inferred from the opinion of the Board member, for the first time see the Hopkins or Belridge property a few weeks before the trial, but he did go upon the property a few weeks before the trial to confirm facts known to him during the years 1910 and 1911. The witness Johnson on the basis of his scientific education and experience and based upon his experience as an advisor to purchasers of oil lands, his intimate knowledge of the territory and of the values therein and of the discovery of Van Slyke testified that the Hopkins property on January 25, 1911 had a fair market or actual cash value of \$2,900,000.00. [R. 127.] In making such an estimate of value, using both his practical and scientific training and experience, the witness Johnson eliminated from his mind entirely the developments of the Belridge property subsequent to 1911. [R. 129.] The witness Johnson further testified that in 1911 he would have recommended to a purchaser that \$2,900,000.00 be paid in cash for the property. The witness Johnson further testified from a geological standpoint as well as from the standpoint of a practical oil operator and as a practical

purchaser of prospective oil land, the judgment and conclusion which Burton E. Green and Whittier came to as to the value of this property was more than justified. The member of the Board [R. 30] seeks to discount the value of the testimony of the witness Johnson on two grounds—first, that he visited the property only a short time before the trial of the case, and secondly, that his estimate of value was based entirely upon his geological education and observation and was purely theoretical in character.

The record entirely fails to support either of said conclusions. The record conclusively shows that Johnson was thoroughly familiar with the Belridge property in the year 1911 as well as property adjacent thereto and that he visited the property a short time before the trial of this case to refresh his memory as to the facts and conditions known to him to have existed in the year 1911. The record further refutes the conclusion that the witness based his estimate of value entirely upon his geological training and experience and that it was theoretical in character. It is true that the witness Johnson was a geologist in the year 1911, a competent one, and that he used such training in determining his value, but it is furthermore true and most important to observe that the witness Johnson in the year 1911 and since that date has been engaged in the business of advising prospective oil purchasers as to lands and he testified [R. 122], that numerous sales were made as well as purchases based upon his conclusions and recommendations in the premises, and he testified that he used the sum total of all of his training and experience, both academic and practical, in arriving at his conclusion of value.

The member who heard the testimony of the witness Johnson reached a conclusion at variance with the opinion of the Board member. See dissenting opinion. [R. 47.]

The cross-examination of the witness Johnson did not disturb either his qualifications or estimate of value nor demonstrate that there entered into his opinion erroneous facts or conclusions.

It is respectfully submitted that the Board member erred in his conclusion with respect to the weight to be given to the testimony of the witness Johnson and his opinion with respect thereto is contrary to the evidence.

The Witness W. W. Orcutt.

The witness Orcutt is a geologist of recognized standing who has been connected with the Union Oil Company of California and has been so employed by them since the year 1897. The witness is a graduate of Stanford University where he majored in geology. [R. 131.] During the years 1910 and 1911 and prior thereto the witness Orcutt gained familiarity with oil properties and prospective oil properties in Southern California and was familiar with the Belridge property during the year 1911 as well as properties adjacent thereto. The Union Oil Company is a large and representative oil company operating in California and in the years 1910 and 1911 the witness Orcutt advised the Union Oil Company with respect to its purchases and sales of oil properties in California. [R. 132.] The witness Orcutt inspected the property of the Belridge Oil Company shortly before the trial of the case for the purpose of verifying and refreshing his memory with respect to the facts and conditions

known to him to have existed during the years 1910 and 1911, and particularly to verify the discoveries which Van Slyke made during the year 1910. The witness Orcutt gave as his estimate of value that the Belridge Oil property on January 25, 1911, had an actual cash value of \$2,700,000.00, and testified that in 1911 he would have recommended to his employer, the Union Oil Company, that they pay the sum of \$2,700,000.00 for the Belridge Oil property. [R. 133.]

The member of the Board writing the opinion in this case apparently discounts the testimony of the witness Orcutt on two grounds—first, that his estimate was a theoretical one, giving emphasis to his geological training, and secondly, that he visited the property only a short time before the trial of the case. As in the discussion of the testimony of the witness Johnson, it is likewise true in the instance of the witness Orcutt that both conclusions of the Board are in error. The witness Orcutt was shown to have had practical and actual experience in the vicinity of the Belridge property in the years 1910 and 1911; he was shown to have been the responsible purchasing officer for a large and representative oil company in California in the years 1910 and 1911, and both prior and subsequent thereto, and his opinion of the actual cash value of the Belridge property was not based entirely upon his geological training and experience, but based upon the practical experience which he had had as one having to do practically and actually with the purchase and sale of prospective oil properties during the years 1910 and 1911. [R. 134 and 135.] -

The witness Orcutt did not go upon the Belridge property a week or so before the trial of the case for the

purpose of then becoming for the first time familiar with the condition of the property but inspected the property a short time before the trial of the case in order to confirm and refresh his memory with respect to conditions known to him to have existed during the years 1910 and 1911.

The Board member who wrote the opinion in this case has misinterpreted the occasion for the testimony with respect to the visit of both the witness Johnson and Orcutt to this property a short time before the trial. They went upon the property and inspected it to refresh their memory and their knowledge with respect to conditions that existed in 1910 and 1911. Had it been shown that the discoveries of Van Slyke were not actual but were only visionary and potential—the discoveries which he reported to Green and Whittier and upon which they acted, his discoveries might have been discounted as being nothing more than a vision with respect to possibilities, but Johnson and Orcutt testified that it was now possible to verify the discovery which Van Slyke made. They both testified that any practical oil man would have been justified in concluding as did Green and Whittier with respect to the discoveries which Van Slyke made.

There was further introduced Exhibit 5 which shows the dates upon which the oil wells were drilled on the Belridge property and the testimony shows [R. 112] that the first oil well was drilled where Van Slyke had made his discoveries.

It is not shown that in any respect the testimony of the witnesses Johnson or Orcutt should be discredited. The Board member does not attack their qualifications and they are not shown to have had any interest in the out-

come of this proceeding and in fact, the witness Orcutt was in 1911 and is now identified with a competitor of the petitioner corporation.

The testimony of the three experts was consistent, reasonable and stands uncontradicted. Their conclusions were not attacked nor shown to be in error on cross-examination and the Board member who heard their testimony stated that their sincerity, candor and intelligence was unchallenged, and that he was persuaded and convinced thereby. [R. 38.]

In conclusion, therefore, on this aspect of the case, it is submitted that the Board member erred when he disregarded the substantial and uncontradicted evidence of the three experts here in question.

(c) TESTIMONY OF THE THREE EXPERTS IS SUPPORTED
BY OTHER EVIDENCE.

Petitioner did not offer alone the expert testimony of the witnesses Green, Johnson and Orcutt, but in addition thereto submitted other evidence which it is contended corroborates and supports the expert testimony thus given.

It is not challenged that the Belridge property was an immensely valuable property, neither is it challenged that oil was discovered exactly in the place where Van Slyke had made his discovery. Neither is it challenged that Green and Whittier and the others instrumental in the organization of the corporation acted wisely with respect to the acquisition of the option. [R. 112—Exhibit 5, and R. 122.]

Representative sales and purchases if they be within the territory involved, often prove helpful and are com-

petent to test the accuracy of the testimony of experts. The petitioner in an effort to supply collateral and corroborative evidence of value introduced a purchase made by the Associated Oil Company in the year 1911 of property in the immediate vicinity and comparable, though not as valuable, as the Belridge property. This was a purchase of 23,962 acres of land for a cost price of approximately \$1,600,000.00. Certainly such a purchase has to be representative in character. The Associated Oil Company, Exhibit 2, purchased property very near the Belridge property in the year 1911 at a cost of \$66 $\frac{2}{3}$ per acre. [R. 73, 75.] The record shows that the property purchased by the Associated Oil Company was similar to the Belridge or Hopkins property but was not as favorably located with respect to producing fields or with respect to anticlines. It is shown that the property purchased by the Associated Oil Company was valuable as prospective oil land and that prior to the purchase thereof in 1910 by the Associated Oil Company, oil had not been discovered on the property. [R. 115—Exhibit 6, R. 172, 129 and 130.] The witness Johnson gives as his conclusion that the Associated Oil property was not as valuable prospective oil property as was the Belridge Oil property and states his reasons in the following language:

“By maps which I use I am able to locate the property which the Associated Oil Company purchased in 1910 and referred to in Exhibit 2 in evidence in this case. The property which the Associated Oil Company purchased, as before mentioned, was not in as good prospective oil territory as the Belridge oil property.

A. From what I know of the position of that property as you have described it, I would say it

was not in as good territory, and I can give my reasons for that, very briefly.

Q. Do so, please.

A. In my investigation of the general region in December of 1908, in the preparation of Bulletin No. 416, Mr. Arnold and I found that the evidences of oil in the croppings in the foothills of the district to the southwest of the Lost Hills—and when I say ‘foothills’ I mean the foothills of the Temblar—the evidences of oil were less specific, less definite, that is the oil sands and croppings were less heavily impregnated with oil, that is the oil shales in which they originated, were less heavily impregnated with oil than some of the rocks in the region lying further to the southeast, especially in the region around Gould Hills, which represents the nearest foothill territory to the Belridge property. In this Gould Hills area there are very extensive showings of oil sands and oil shales which were part of the basis that I used in determination of value and that is the reason why I considered the property purchased by the Associated Oil Company, lying generally to the northwest of the Hopkins property as less valuable for oil than the lands which the Belridge Company acquired.” [R. 129, 130.]

The dissenting opinion filed in this case [R. 45], concludes that the property of the Belridge Oil Company was more valuable than the property which was purchased by the Associated Oil Company and gives most cogent and satisfactory reasons therefor.

The evidence further shows that shortly after the petitioner corporation was organized and before oil was discovered upon the Hopkins or Belridge property, that one

of the stockholders, Michael J. Connell refused a cash offer from Whittier in the amount of \$500,000.00 for his stock in the corporation. While it is true that the sale was not consummated, nevertheless it shows the value attaching to the stock before there was discovery of oil on the property. The offer is testified to by both Connell and Green. Connell owned one-fifth of the stock of the corporation and his holdings, therefore, represented a minority interest. The Board discounts this testimony with the conclusion that the transaction did not sufficiently crystalize to be regarded as more than a trifling indication of value. We admit that standing alone this offer would not be conclusive proof of value but it was introduced in evidence and made a part of the record as one of the further corroborating bits of evidence to show that the value testified to by the witnesses, Green, Johnson and Orcutt was reasonable in all respects.

The evidence also shows that W. J. Hole found it necessary to pay \$125,000.00 in cash to a cousin of Mrs. Hopkins to secure his good offices in obtaining the option and that he paid \$35,000.00 in cash to an agent of Mrs. Hopkins to assure his good offices to the end that the option might be obtained and that he agreed to give to one Hill, the agent of Mrs. Hopkins, one-fourth of the stock which he, Hole, would receive when the corporation was organized. It is certainly not reasonable to presume or conclude that a businessman would have paid the sum of \$160,000.00 in cash and agreed to part with one-fourth of his stock to obtain an option on the property as to which the person obtaining the option was only to pay the sum of \$25,000.00, and there would be no certainty with respect to the corporation's exercising the option once it

had secured it. This large expenditure by Hole is but another corroborating circumstance and fact to lend support to the value of the option as given by the expert witnesses. But again this bit of evidence is disregarded by the Board member. It is significant to note that the Board member does not discuss this feature of the testimony or give it any value whatsoever as a supporting bit of evidence to the testimony of the experts as to values.

It is respectfully submitted that the additional proof of value herein recounted when combined with the uncontradicted testimony of three qualified experts was certainly substantial evidence which the Board member should not have disregarded and the disregard of the same by the Board member constitutes error.

(d) THE VALUE OF THE OPTION WAS DETERMINABLE
BY THE EVIDENCE.

The Board member writing the opinion suggests that the witnesses testified as to the value of the land but did not testify as to the value of the option. [R. 33.] The testimony in the case is replete with the fact that it was the common custom in purchasing oil lands in Southern California during the year 1911 to acquire them by option. It would seem almost elemental that an option to purchase property would be worth the difference between the price called for in the option and the actual cash value of the property upon which the option is held. If an individual has an option to purchase a dollar by the payment of fifty cents and the question at issue is what is the option worth, and the evidence shows that the dollar is worth one hundred cents, it would seem elemental that the option has a value inuring in it of the difference between

the amount to be paid under the option and the actual cash value of the article covered by the option. This method of computing the value of an option has frequently been used by the Board of Tax Appeals in determining the value of an option. See *Decision of Karl Van Platen v. Commissioner*, 10 B. T. A. 250; *Robert Brunton Studios, Inc. v. Commissioner*, 15 B. T. A. 727; *Belmont Shore Company v. Commissioner*, 21 B. T. A. 714; *Realty Sales Company v. Commissioner*, 10 B. T. A. 1217, and *United Studios, Inc. v. Commissioner*, 15 B. T. A. 737.

In the case of the *Belmont Shore Company v. Commissioner*, *supra*, the question at issue was the value of an option for which capital stock was issued. The option related to certain land located in the vicinity of Long Beach, California. The option when acquired had cost nothing of value but was assigned to the corporation for a consideration of \$60,000.00. The Board found that the stock for which the option was issued had a value of \$60,000.00 and of course found that the option itself had a value of \$60,000.00. The facts upon which the value of the option in the case at bar could be determined were in evidence and it was not necessary or indeed proper for the witnesses to make mathematical calculations while on the witness stand. The evidence shows that the witnesses were familiar with options and that it was the practice to take options on prospective oil properties. [R. 101.] It was shown that the option in question which is in dispute was an unusually favorable option. [R. 85.] It is submitted that the value of the option is established by the evidence which shows the actual cash value of the property and the price at which the property could be purchased under the terms of the option. For the Board.

member to disregard the evidence upon such grounds, if he did so, would be error and would be the injection of a harsh rule beyond the power of the member. See *Chicago Railway Equipment Company v. Blair* (C. C. A.-7), 20 Fed. (2d) 10.

The question of the determination of the value of an asset for invested capital purposes is one which has occurred before the Board with frequency and has also been the subject of decisions of several of the Circuit Courts of Appeal with respect to the decisions of the Board.

The Circuit Court of Appeals for the Eighth Circuit in the case of the *Sioux City Stock Yards Company v. Commissioner*, 59 Fed. (2d) 944, had before it the valuation of certain contract rights for the purpose of determining the invested capital of the corporation for the years 1918, 1919 and 1920. The Board denied the value as claimed by the petitioner, but the Circuit Court in a well reasoned opinion held that the contract should be included in invested capital as contended for by the corporation.

The United States District Court for the Northern District of Ohio in *Service Recorder Company v. Routzahn*, 24 Fed (2d) 875, had before it a decision of the Board of Tax Appeals with respect to the years 1919 and 1920, wherein the Board had sustained the Commissioner of Internal Revenue and refused to permit the corporation to include in its invested capital the cash value of certain patent licenses for which stock was issued. Here again the District Court reversed the decision of the Board and held that the value as contended for had been proven, stating among other things the following:

“The value of a thing is not always and solely to be determined by precise mathematical computation based upon cash exchanged therefor; and values are sometimes enhanced by faith in the ultimate future of the thing for which those having such faith are willing to hazard their time, money and effort. This is more particularly true in the case of patent licenses, although it may in many cases be applicable to tangibles, such as real estate purchased in anticipation and expectation of development and improvements. Within sound limits, the judgment and expectation of those assuming the risk are elements entering into a determination of value.”

The Circuit Court of Appeals for the Sixth Circuit in the case of *Rookwood Pottery Company v. Commissioner*, 45 Fed. (2d) 43, had before it for consideration the determination of the invested capital of the corporation. The Commissioner of Internal Revenue had excluded from invested capital the sum of \$16,000.00 represented by stock which had been issued for certain intangibles. Here again the Circuit Court of Appeals reversed the Board and found that the amount of capital stock issued for the intangibles should have been included in the invested capital and that the intangibles were worth a cash value, and stated among other things:

“We see no reason why the taxpayer did not make its case when it put in proofs clearly and distinctly tending to show this value; and when the proofs so introduced remained unchallenged by contrary proofs or by destructive analysis, it was the duty of the commissioner to decide the issue in accordance with the proof then appearing before him; and it was, we

think, the duty of the board to take the same view. The Blackstonian 'certainty to a common intent' ought to be sufficient."

See also the decision of the District Court of Massachusetts in *Arizona Mining Company v. Casey*, 32 Fed. (2d) 288, wherein the court allowed a paid in surplus for invested capital purposes of \$2,000,000.00

We frequently find the Commissioner of Internal Revenue taking the opposite position to that taken in the case at bar and contending that the decision of the Board is at variance with the substantial evidence if the decision be adverse to him. A striking example is accorded in the case of *Commissioner of Internal Revenue v. Swenson*, 56 Fed. (2d) 544, in which was involved the question of the fair market value of stock received in exchange for certain oil lands. The Board of Tax Appeals determined that the stock did not have a fair market value and consequently the taxpayer should not account for tax upon the receipt of the stock until it was sold by him. The Commissioner appealed the case to the Circuit Court of Appeals for the Fifth Circuit which reversed the decision of the Board wherein the Commissioner successfully contended that the Board had decided the case at variance with the substantial evidence adduced. The opinion of the Circuit Court of Appeals for the Fifth Circuit is particularly helpful in this case with respect to the discussion of prospective and speculative values and it involved the valuation of oil lands. The court among other thing stated as follows:

"The value of property at a given time depends upon the relative intensity of the social desire for it at that time, expressed in the money it would bring

in the market. That value depends largely on expectations as to what may be realized from the property in the future. *Ithaca Trust Co. v. United States*, 279 U. S. 151, 49 S. Ct. 291, 73 L. Ed. 647. The fact that those expectations are highly speculative may not keep them from being influential in bringing about a willingness to expend money for the acquisition of the property or an interest in it. Though a venture is as speculative as a lottery, a chance or interest in it may be readily saleable for a substantial sum of money. The law does not forbid the recognition of the proved exchangeable value of an asset because of the speculative nature of it. *Collin v. Commissioner of Internal Revenue (C. C. A.)*, 32 Fed. (2d) 753. Furthermore, it did not appear from the evidence that it was mere guesswork to attribute a substantial money value to the shares of stock in question at the time they were received in exchange for an oil and gas lease. At and prior to the date of that exchange, there were extensive explorations and oil developments of nearby lands located on all sides of the tracts covered by the leases held by the corporation. Under the conditions shown by the evidence to have existed at the time those shares were acquired by the taxpayer, it was not to be assumed that those operations had not resulted in the acquisition of knowledge of facts furnishing a substantial basis for a reasonable belief that oil in paying quantities would be found in land included in those leases."

The Circuit Court of Appeals for the Eighth Circuit in *Planters Operating Company v. Commissioner*, 55 Fed. (2d) 583, had before it for decision the value to be assigned to a lease respecting certain hotel property located in St. Louis, Missouri. Capital stock had been

issued for the lease in question. The Commissioner of Internal Revenue had assigned no value for the lease in question and the Board of Tax Appeals upheld the determination of the Commissioner. The court in reversing the Board of Tax Appeals did so on the following grounds:

“On the hearing before the Board of Tax Appeals, petitioner introduced the testimony of three disinterested witnesses, experienced hotel managers, all of whom testified that there was value in the lease when it was acquired by petitioner in November, 1918, amounting to at least \$200,000. They explained how they arrived at this conclusion. Their reasons were couched, not, perhaps, in technical scientific terms, but in the language of laymen. Their testimony was uncontradicted.

“The Board of Tax Appeals gave no weight to this testimony because it considered that it was based upon an erroneous understanding by the witnesses of the real terms of the lease.”

(e) PRESUMPTION ESTABLISHED BY FORMER DECISION OF THE BOARD IN 11 B. T. A. 127 IS OVERCOME BY THE EVIDENCE IN THE CASE AT BAR.

The opinion of the Board member in the case at bar seems to be influenced somewhat by a prior decision of the Board reported at 11 B. T. A. 127. It is clear that the prior decision of the Board is not *res adjudicata* with respect to this proceeding and the Board member who wrote the opinion admits the same. [R. 26.] See, also: *Union Metal Manufacturing Company v. Commissioner*, 4 B. T. A. 287.

There is of course a presumption that the former decision of the Board was correct but as pointed out by the member who prepared the dissenting opinion [R. 52], the evidence adduced at the trial of the case at bar, bears but small resemblance to the evidence adduced as a result of which the Board rendered its decision in 11 B. T. A. 127. The evidence presented at the trial of the case at bar is conclusive with respect to the deficiencies in proof pointed out by the Board in the evidence when the case was tried before it and as a result of which it prepared its opinion in 11 B. T. A. 127. We submit that the dissenting opinion so sufficiently answers this contention that it is not necessary to further dwell upon this point.

When the case was tried before the Board resulting in the opinion reported in 11 B. T. A. 127, it was tried at a time when, as one Circuit Court has expressed it, a trial before the Board was merely a preliminary skirmish for the reason that if the taxpayer was dissatisfied with the decision of the Board it could pay the tax, file a claim for refund, bring suit in the United States District Court and try its case over again, and this, in fact, is the exact situation in which the prior decision of the Board now finds itself.

5. It Is Reversible Error for the Board of Tax Appeals to Disregard Competent Relevant Testimony When It is Uncontradicted.

The above heading is quoted from the opinion of the Circuit Court of Appeals for the Eighth Circuit in the case of *Planters Operating Co. v. Commissioner*, 55 Fed. (2d) 583, and is a rule which is well established both by the decision of this Honorable Court and by the Circuit Courts of Appeal of other circuits. This Honorable

Court has not hesitated to require strict compliance with this rule that unimpeached and uncontradicted evidence cannot be disregarded and has reversed the Board upon that ground in the following cases: *Citrus Soap Co. v. Commissioner*, 42 Fed. (2d) 372; *Buena Vista Land & Dev. Co. v. Lucas*, 41 Fed. (2d) 131, and *Royal Packing Co. v. Commissioner*, 22 Fed. (2d) 536.

In the *Citrus Soap Co. v. Commissioner (supra)* this Honorable Court reversed the Board for failure to give proper consideration to the evidence. A witness who was a director, secretary and treasurer of a predecessor corporation testified that the good will acquired by the petitioner from the predecessor company had a value of approximately \$50,000.00. The Board, however, disregarded this evidence and ruled that the good will had no value. This court, in reversing the Board, and in referring to the testimony of the witness above mentioned, stated:

“The foregoing testimony was competent and from a competent source. It was not contradicted by any other testimony. It was not unreasonable or improbable in itself, and, in our opinion, it tended to prove as a matter of law that the good will acquired by the petitioner from its predecessor in interest had a substantial value. What that value was, or the mode or formula by which it should be ascertained, is primarily for the determination of the Board of Tax Appeals.”

In *Buena Vista Land & Dev. Co. v. Lucas (supra)*, this court stated:

“It was proved that the land involved in the transaction was worth about \$25,000,000 on March 1,

1913, and was worth as much or more at the time of the settlement. The question with which the Board of Tax Appeals concerned itself was the relative market value of the property at the time of its sale, or surrender, and its value on March 1, 1913. The Board announced that it would fix the tax upon the difference between the two.

It was thus the duty of the Board of Tax Appeals to ascertain the value of the property disposed of June 28, 1921, as of the date of March 1, 1913 (section 907(b), 44 Stat., Chap. 27, pp. 9, 107), and fix the same in its findings. This the Board failed to do and for this error its decision must be reversed. *Kendrick Coal & Dock Co. v. Commissioner of Internal Rev.* (C. C. A.), 29 F. (2d) 559; *Pfleghar Hdw. Specialty Co. v. Blair* (C. C. A. 2), 30 F. (2d) 614; *Chicago Ry. Equip. Co. v. Blair* (C. C. A. 7), 20 F. (2d) 10. * * *.”

The rule has been applied in other circuits in the following cases: *Conrad & Co. v. Commissioner* (C. C. A. 1), 50 Fed. (2d) 576; *Bonwitt Teller & Co. v. Commissioner* (C. C. A. 2), 53 Fed. (2d) 381; *Pflegher Hardware Specialty Co. v. Blair* (C. C. A. 2), 30 Fed. (2d) 614; *Boggs & Buhl, Inc. v. Commissioner* (C. C. A. 3), 34 Fed. (2d) 859; *Pittsburgh Hotels Co. v. Commissioner* (C. C. A. 3) 43 Fed. (2d) 345; *Nichols v. Commissioner* (C. C. A. 3), 44 Fed. (2d) 157; *Chicago Rwy. Equip. Co. v. Blair* (C. C. A. 7), 20 Fed. (2d) 10; *Planter's Operating Co. v. Commissioner* (C. C. A. 8), 55 Fed. (2d) 583; *Dempster Mill Mfg. Co. v. Burnet* (Ct. of App. D. C.), 46 Fed. (2d) 604.

In *Nichols v. Commissioner* (*supra*) the court summarized the testimony and stated:

“This testimony overcame the presumption arising from the determination of the Commissioner. The burden then shifted to the Commissioner to support his determination by evidence, and this he did not do nor attempt to do, and accordingly his determination cannot stand. *United States v. Rindskopf*, 105 U. S. 418, 26 L. Ed. 1131; *Thompson Pottery v. Routzahn* (D. C.), 25 F. (2d) 897; *Flannery v. Willcuts* (C. C. A), 25 F. (2d) 951; *Briggs Manufacturing Co. v. United States* (D. C.), 30 F. (2d) 962.

The Board of Tax Appeals disregarded all the positive and affirmative evidence in the case. Its own findings are not predicated upon any substantial evidence, and therefore its redetermination is set aside, the determination of the Commissioner reversed, and the income tax returns of the petitioner approved.”

In *Dempster Mill Mfg. Co. v. Burnet*, *supra*, the Board disregarded the testimony of an expert witness on the ground that he was an interested witness. Upon reversing the Board the court stated: “We think it was error to disregard the testimony of this witness inasmuch as it stands uncontradicted.”

The instant case comes directly within the rule of the above cited cases. There can be no doubt that the witnesses were qualified. Their testimony was reasonable and consistent and was uncontradicted. There is no reason whatsoever for discrediting their testimony for two of them were disinterested parties and there is nothing to indicate that the third witness' interest in any way affected

his testimony, and interest alone is not sufficient to justify the disregard of his testimony. *Dempster Mill Mfg. Co. v. Burnet, supra*. The Board specifically states in its opinion that it has not relied upon its own knowledge and experience. [R. 37.]

In addition to the foregoing, in the instant case, there were three witnesses, while in the *Citrus Soap Co. v. Commissioner, supra*, and the *Dempster Mill Mfg. Co. v. Burnet, supra*, there was only one. Furthermore in the instant case the Board member who conducted the hearing was highly impressed with the candor, earnestness, sincerity and intelligence with which the witnesses testified. [R. 38.] This fact alone should be sufficient to make the disregarding of the testimony by the member of the Board reversible error, *Jewett & Co. v. Commissioner* (C. C. A.-2), 61 Fed. (2d) 471.

It is submitted that the disregard by the Board member of competent, relevant and uncontradicted testimony was reversible error.

CONCLUSION.

In conclusion it is respectfully submitted that the decision of the Board of Tax Appeals is not supported by substantial evidence.

That it was reversible error for the Board of Tax Appeals to disregard the competent and uncontradicted testimony of the witnesses.

That the evidence conclusively establishes the actual cash value of the option to be at least equal to the value of the stock issued therefor or \$1,000,000.00.

Wherefore, it is respectfully submitted that the decision of the Board should be reversed and that such other and further relief be granted as this Court deems proper.

Respectfully submitted,

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